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No. 290

Supreme Court of the United States

October Term, 1948.

WILLIAM J. MINSCH, *et al.*, Intervenors, RAILWAY AND LIGHT SECURITIES COMPANY; the MASSACHUSETTS GENERAL HOSPITAL; and BOND INVESTMENT TRUST OF AMERICA, Intervenors,

Petitioners,

—v.—

FRANK BAILEY, *et al.*,

Respondents.

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

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Unless otherwise indicated by the context, references are to pages of the Transcript of Record.

Preliminary Statement

Petitioners apply for a writ of certiorari to the United States Circuit Court of Appeals, First Circuit, to bring up for review the judgment of said court reversing a decree of the District Court for the District of Massachusetts, which decree directed receivers of Aldred Investment Trust (hereinafter referred to as "Aldred") to pay Debenture Holders of Aldred a call premium in the amount of 5% of the face value of their debentures (14).

The Question Presented

The "Questions Presented", as set out in Petitioners' brief (p. 6), hardly present an accurate statement of the issue involved.

There is but a single question presented and that is: Where a Massachusetts Trust issued debentures under an Indenture which provides that a premium shall be paid to debenture holders if there be a "redemption at the option" of the Trust, are debenture holders entitled to the premium if the debentures are paid off pursuant to an order of the court, entered over the opposition of the Trust, directing receivers of the Trust to liquidate it?

It should be noted at the outset that there is an elemental fallacy in Petitioners' position, to wit, the assumption that we are dealing here with a corporate "reorganization," and with the discretionary powers incident to such a proceeding.

The judicial power to effectuate a corporate "reorganization" is exercised by means of one of two techniques. The first, and older, technique is the equity receivership. In such a reorganization a plan must be presented to the Court on notice to creditors and security holders; the creditors and stockholders must be given an opportunity to vote on the plan; and if the plan is approved by the Court, the assets are transferred to a new corporation in accordance with the terms of the plan.

No such proceeding has taken place here.

The second judicial technique finds expression in former Sections 77 and 77B and Chapters X and XI of the Bankruptcy Act, and similar statutes. But even under this statutory technique, the basic principles of reorganization remain the same; there is still the necessity for a plan, its

submission to stockholders and security holders; a vote, and Court approval. All that is eliminated in the second method is the sale to a new corporation.

There has been no such statutory reorganization here.

Plainly, we are dealing here with a partial liquidation, and not with a "reorganization," and any attempt to transform what occurred here into a "reorganization" must founder on fact that all reorganization plans which were proposed were duly rejected by the Court, and that in what was finally done none of the steps requisite to a reorganization was taken.

Facts

Aldred was organized in 1927 as a Massachusetts Trust.

In 1944, the Trust had outstanding $5,900,000. face amount of 4½% debentures maturing in 1967. To each debenture were attached ten shares of non-par common stock for each $1,000. of principal amount of the debenture, so that 59,000 such "attached" shares were outstanding. In addition, there were outstanding 112,500 common shares, not attached to debentures, and referred to as "free" common shares.

In May, 1944, the Securities & Exchange Commission (hereinafter referred to as "S. E. C.") brought this suit in the District Court of the United States for the District of Massachusetts against Aldred and its former management, the "Hanlon Group". The complaint alleged gross misconduct and gross abuse of trust on the part of the Hanlon Group, resulting in the dissipation of the assets of the Trust. The relief sought was an injunction against further participation by the Hanlon Group in the affairs of the Trust and the appointment of a receiver to take over the assets of the Trust, and "for liquidation and distribution to

such creditors, debenture holders and shareholders of the Trust as may be entitled thereto."

Aldred and the Hanlon Group interposed answers denying all the material allegations of the complaint.

The case was tried before District Judge Sweeney. In his Findings of Fact and Conclusions of Law (*S. E. C.* v. *Aldred,* 58 F. Supp. 724), Judge Sweeney found, among other things, that the value of the assets of the Trust were, and for years prior thereto had been, less than the principal amount of the outstanding debentures, and its earnings insufficient to meet the interest requirements thereon; that the Hanlon Group had been guilty of gross misconduct and gross abuse of trust; that they had ventured "the debenture holders' money" in speculative ventures without notice to, and in violation of, the rights of the debenture holders; that the Hanlon Group, by paying interest on the debentures out of capital, had avoided a technical default under the Indenture and

> "The debenture holders are left helpless under the terms of the debenture agreement to halt the dissipation of their assets."

On January 19, 1945, judgment was entered, ousting the Hanlon Group and appointing receivers with power to operate the Trust. *S. E. C.* v. *Aldred, supra.*

On June 19, 1946 District Judge Sweeney rendered a judgment directing, among other things, that the Receivers "proceed to liquidate the Trust" (R. 32).

On June 19, 1947 Judge Sweeney denied an application of the debenture holders for payment of the "call" premium, and entered an order directing the Receivers to pay the outstanding debentures at their face amount plus accrued interest through June 30, 1947 (R. 31).

This order has been carried out: the debentures have been surrendered to the Trust, and the debenture holders have received the face amount of their debentures plus accrued interest to June 30, 1947, together with new certificates of common stock to replace those which were attached to the surrendered debentures.

The receivership suit was contested by the Trust and the Hanlon Group. When judgment went against them, and Receivers were appointed, they appealed to the Circuit Court of Appeals, and after that Court affirmed the judgment, they applied unsuccessfully to this Court for a writ of certiorari (*Aldred Investment Trust* v. *S. E. C.*, 151 F. 2nd 254; Certiorari denied, 326 U. S. 795).

While that application was pending, these Respondents acquired the 110,000 free shares which had been owned by the Hanlon Group and, in addition, $79,000 of debentures with 790 shares of common stock attached. This acquisition was by bona fide purchase, at arms' length, and since then the Hanlon Group has had no relation whatsoever to the Trust or to Respondents.

From the time Respondents acquired their stock in the Trust, they made every effort to prevent liquidation and payment of the debentures. In each of these efforts they were successfully opposed by the debenture holders who, on every occasion, pressed for liquidation and payment of their debentures.

In February, 1946, Respondents moved to terminate the receivership and restore the assets of the Trust to its trustees on the ground that the corrupt Hanlon Group had been ousted, the Trust had become solvent, and the debenture holders were amply secured.

The debenture holders joined with others in opposing that motion, and Judge Sweeney denied it (R. 11).

Respondents then moved to reorganize the Trust in certain respects, with no change, however, in the outstanding debentures and no diminution of the rights and priorities of the holders thereof.

The debenture holders joined in opposing that motion; they pressed for liquidation of the Trust and payment of the debentures, and Respondents' motion was denied.

At the same term, i.e., in April, 1946, Respondents made another motion for the termination of the receivership and the restoration of the property of the Trust to its trustees.

Again the debenture holders joined in opposition to the motion, insisting upon liquidation and payment of the debentures, and again Respondents' motion was denied.

Respondents made similar motions in June, 1946; again the debenture holders joined in opposing them, and again the motions were denied, this time with an order directing the Receivers "to proceed to liquidate the Trust." From that order Respondents appealed to the Circuit Court of Appeals, where the order was affirmed (*Bailey* v. *Proctor*, 160 F. [2d] 78; Certiorari denied, 331 U. S. 834).

In affirming that order, the Circuit Court rendered an opinion replete with expressions which emphasize that the payment of the debentures was ordered over the objection and opposition of Aldred, and not as the result of the exercise of any right or option on the part of Aldred.

In justification of the debenture holders' right to receive their money, the Circuit Court of Appeals pointed out (pp. 82-83) that the solvency of the Trust might be "temporary" and "transient"; that

> "the vagaries of the stock market are familiar to all of us,"

and that

> "There seems to be doubt also as to the ability in the future of any portfolio to earn these interest requirements except by resort to speculative securities with the hope of capital appreciation."

The Circuit Court agreed with the Court below (p. 83):

> "that the debenture holders were entitled now to the cash salvaged from what had appeared to be a doomed enterprise"

and that

> "it would be inequitable to allow them [Respondents] to force those with burnt fingers to remain investors in an enterprise of proven questionable value."

Thus it is clear that Aldred did not instigate, abet or acquiesce in the proceedings which brought about the order for payment of the debentures. On the contrary, as appears from the proceedings outlined above, Aldred, through its controlling shareholders, made every possible effort to prevent liquidation and payment of the debentures, and in every instance these efforts were strenuously, and successfully, opposed by the debenture holders, who insisted that Aldred be compelled by Court order to pay the debentures. The significance of this is plain: the payment of the debentures was accomplished by judicial decree over the opposition of Aldred, and in no way represents the exercise of any right, option or election on Aldred's part.

After the debentures had been paid pursuant to the order of the Court, and all debts except administration expenses had been paid in full, these Respondents moved to

supplement the judgment of liquidation by an order permitting those stockholders who should so elect in writing, to continue the Trust with their distributive shares as its capital. The Receivers, the Securities and Exchange Commission, and the attorneys for the debenture holders' Committee all appeared before the District Judge on the return of that motion. The Receivers and the Commission stated that they had no objection to the granting of the motion. The attorney for the Committee, although present at the hearing, made no statement to the Court. He had previously advised the attorneys for Intervenors that the Committee had no objection to the granting of the motion. There was no suggestion that any premium for "redemption" would become payable.

On November 6, 1947, the learned District Court made an order denying that motion and authorizing the Receivers to make partial distribution to stockholders. The operation of that order was stayed by the Circuit Court of Appeals pending appeal, and, on appeal, that Court reversed the order with an opinion in which the Court said:

> "All the former objections to the continuation of the Trust have been removed. The debenture holders have been paid in full; thus, there is no question of the shareholders speculating with other people's money. All shareholders who desire to withdraw may be allowed to do so and will receive their full pro rata share.
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> "Since no one will be injured, we see no reason not to allow the present equitable owners of the Trust property to decide what to do with their money."

Bailey v. *Proctor,* 1 Cir., 1948, 166 F. 2nd 392, 396.

The Circuit Court of Appeals left open for decision by the District Court, in the first instance, the question whether or not, in view of the modification of the order of liquidation, debenture holders are entitled to receive the call premium on their debentures (R. 33).

The Committee representing debenture holders then moved for an order directing the Receivers to pay a call premium of 5% to the persons who had surrendered, or would thereafter surrender, their debentures (R. 1).

From the order granting that motion (14) (*S. E. C.* v. *Aldred,* 76 F. Supp. 614), respondents appealed to the Circuit Court of Appeals, which unanimously reversed and remanded (45-6) with an opinion (40-45). *Bailey* v. *Minsch,* 1 Cir., 1948, 168 F. 2nd 635.

It is to review the last mentioned determination that Petitioners seek certiorari.

POINT I

Any contractual right to the call premium on the redemption of debentures must be found in the Indenture pursuant to which they were issued. The Indenture, in clear and unequivocal language, gives the right to a call premium only when redemption is effected "at the option" of Aldred. The redemption which occurred here was not effected "at the option" of Aldred; on the contrary, it was pursuant to judicial decree entered over the strenuous opposition of Aldred. Hence the call premium is not payable.

Insofar as any contractual right to a call premium is concerned, it must be found, if at all, in the Indenture pursuant to which the debentures were issued.

The only provision of the Indenture for a call premium is that contained in Section 10, which reads:

> "The debentures issued hereunder are subject to redemption at the option of Aldred Investment Trust on any interest payment date prior to maturity as a whole, but not in part, at the principal amount thereof and accrued interest thereon to the date fixed for redemption, together with the premium of 7% of the principal amount thereof if redeemed on or before December 1, 1937 and if redeemed after December 1, 1937, together with premium of 7% of the principal amount thereof less 1% for each full five-year period elapsed since December 2, 1943" (R. 2).

Consequently, insofar as any contractual right to the call premium is concerned, it exists only if payment was effected "at the option" of Aldred.

It needs no argument to demonstrate that the "redemption" here was not effected "at the option" of Aldred. The proceedings leading up to and resulting in the payment of the debentures have been recounted above. They leave no doubt that the Circuit Court of Appeals was entirely correct when it said (43):

> "The bonds were paid as a result of a court order secured at the behest of the bondholders' committee. Payment was made against the express desire of the controlling shareholders who repeatedly sought to have the trust released from receivership with its capital structure intact. The bondholders and Securities Exchange Commission early took the position that the bondholders should not be compelled to leave their funds in the trust to be controlled by the stockholders.

> See our opinion in Bailey v. Proctor, 160 F. (2d) 78. Thus not only did the bondholders not object to payment, but it was at their insistence that the bonds were paid."

In such circumstances, the call premium is not payable (*Otis & Co.* v. *S. E. C.*, 323 U. S. 524 [1945], reh'g den., 324 U. S. 887 [1945]; *Massachusetts Mut. Life Ins. Co.* v. *S. E. C.*, 151 F. (2d) 424 (C. C. A. 8th, 1945), cert. den. 327 U. S. 795 [1945]; *City Natl. Bank & Trust Co.* v. *S. E. C.*, 134 F. (2d) 65 (C. C. A. 7th, 1943); *New York Trust Co.* v. *S. E. C.*, 131 F. (2d) 274, cert. den. 318 U. S. 786 [1943]; *In re North Continent Utilities Corp.*, 54 F. Supp. 327 (D. Del. 1944); *In re Consolidated Electric & Gas Co.*, 55 F. Supp. 211 (D. Del. 1944); *In re Chicago & Northwestern Ry.*, 35 F. Supp. 230, 255 (N. D. Ill. 1940), aff'd 126 F. (2d) 351 (C. C. A. 7th, 1942), cert. den. 318 U. S. 793; *Milwaukee etc. Ry.*, 239 I. C. C. 485, 240 I. C. C. 257, 124 F. (2d) 754, 318 U. S. 523).

As the Court said in *City National Bank & Trust Company* v. *Securities & Exchange Commission*, 134 F. (2d) 85 (C. C. A. 7th, 1943), at pages 68-69:

> "There can be little, if any doubt, so we think, but that the provisions concerning redemption had to do solely with voluntary action on the part of the corporation. The debenture holder was without right to require redemption. That was a right accorded to the corporation, to be exercised solely 'at the option of the company.' It is only upon the exercise of such option that the agreement requires the payment of a premium. Such option lodges in the corporation the discretion to mature the debentures at a date earlier than that otherwise provided. While it is true that

the payment of a premium was a form of compensation to the debenture holders, nevertheless the redemption provision was for the benefit of the corporation, which could be utilized only at its election. The language plainly indicates that the parties did not contemplate that the redemption provision should be effective upon action by the corporation as a result of the Commission's order. *Action under legal compulsion is the antithesis of action by election or 'at the option' of the moving party.*" (Italics supplied.)

Indeed, in *Massachusetts Mut. Life Ins. Co.* v. *S. E. C.*, 151 F. (2d) 424, 429 (C. C. A. 8th, 1945), cert. den. 327 U. S. 795 [1946], the Court had before it the case of a company (Laclede Gas Company) which was not ordered to be liquidated, but which, on the contrary, was merely ordered to retire its senior debt securities, without payment of the contractual redemption premium, as part of a program for reorganization and continued operation as a going business. The Court recognized no difference between a forced liquidation and a forced reorganization, and held that:

"*Submission to a judgment or order of the court or to the requirements of a statute is not a voluntary action in a legal sense.* Compare Dakota County v. Glidden, 113 U. S. 222, 224, 5 St. Ct. 428, 28 L. Ed. 981; Chicago Great Western Ry. Co. v. Beecher, 8 Cir., 150 F. 2d 394. *In a moral or patriotic sense obedience to law may often be regarded as voluntary; but in a legal sense, unless otherwise provided by statute, there is no choice. Submission is coercive.* American Book Co. v. State of Kansas, 193 U. S. 49, 24 S. Ct. 394, 48 L. Ed. 613." (Italics supplied.)

It should be noted that in the foregoing case, Laclede actually *joined* in the application to retire the securities without payment of premium; yet such action was not treated as voluntary.

Petitioners would dismiss the foregoing authorities with the statement that they arose under the Public Utilities Holding Company Act, and are therefore inapplicable to the instant case. They ignore or overlook the fact that these are the very authorities upon which the District Court denied their first motion for the payment of the premium, on June 19, 1947, and that they acquiesced in that order. Certainly, there is nothing peculiar to the Holding Company Act which would justify one rule where securities are involuntarily redeemed in proceedings under the Act and a different rule in other cases.

Moreover, the authorities cited above did not all arise under the Holding Company Act. *In re Chicago & Northwestern Ry.*, 35 F. Supp. 230, 255 (N. D. Ill., 1940), aff'd 126 F. (2d) 351 (C. C. A. 7th, 1942), cert. den. 318 U. S. 793, and *Milwaukee, St. Paul, etc. Ry.*, 239 I. C. C. 485, 240 I. C. C. 257, 124 F. (2d) 754, 318 U. S. 523 arose under former Section 77 of the Bankruptcy Act.

The authorities cannot be distinguished on the ground that they arose under any particular statute; they hold, in the plainest and most comprehensive manner, that indenture covenants for premiums on redemption at the option of the issuer are inapplicable where payment of the security is involuntary. Since this is the law, the former debenture holders could have no contractual right to the call premium.

While petitioners argue that cases arising under the Public Utilities Company Act are inapplicable to the instant case, they refer the Court to *In re Engineers Public*

Service Co., 168 F. 2d 722 (1948). They state that a petition for certiorari is now pending in this Court from the above decision. That case involves no more than an interpretation of the respective statutory functions of the Securities and Exchange Commission and the reviewing court. It is respectfully suggested that while the case involves, among many other things, the payment of a redemption premium to preferred stockholders, the decision is entirely consistent with the authorities cited above. The decision presents no conflict between circuits and no important question affecting the instant case which requires resolution by this Court.

Nor is there any basis for the suggestion (Pet. Brief, p. 11) that the act of the receivers in applying for permission to pay the debentures may be deemed the act of Aldred. What receivers do, they do (*U. S.* v. *Whitridge*, 231 U. S. 144, 149):

> "as officers of the Court, and subject to the orders of the Court; not as officers of the respective corporations * * *. The possession and control of the receivers constituted, on the contrary, an ouster of the corporate management and control, with the accompanying advantages and privileges."

Immediately upon the appointment and qualification of a receiver, said this Court in *Atlantic Trust Co.* v. *Chapman*, 208 U. S. 360, 370,

> "The property passed into the custody of the law, and thenceforth its administration was solely under the control of the Court by its officer or creature, the receiver"

and (pp. 377-378):

> "They [the receivers] are the employes and servants of the Court, and not of the parties."

It was contended by Petitioners in the District Court that the Trustees of Aldred should have redeemed the debentures, and that the act of the Receivers, in paying them, should therefore be deemed merely the act which the recreant Trustees should have performed. The learned District Judge accepted that argument (R. 14), but it is demonstrably untenable and was properly rejected by the Circuit Court of Appeals.

At the time the assets of the Trust were taken out of Aldred's control and placed in the hands of Receivers, and for years prior thereto, Aldred could not have redeemed the debentures, even if it had wished to do so, for the obvious reason, as the Circuit Court of Appeals pointed out on the appeal from the order directing liquidation (160 F. [2d] 78, 80), that

> "from 1937 until sometime subsequent to the earlier proceedings the Trust was insolvent in that the market value of the Trust assets was substantially less than the principal amount of the indentures."

The extent of this deficiency is shown by the Finding of the Trial Court that on June 30, 1944, which was but a month and one-half after the commencement of the action, the asset value per $1,000. debenture was only $643.86, and even that was substantially higher than it had been at any time in the preceding four years.

Thus it is clear that for some years Aldred had been continually financially unable to redeem them, and the

Trustees could not have redeemed them even if they had wanted to.

This inability commenced long prior to the incumbency of the Hanlon Group, and continued without interruption until after the appointment of the Receivers—to be exact, until May, 1946, when the Receivers, under Court direction, sold the stock of Eastern Racing Association. The Hanlon Group did not acquire its stock interest, as the Findings show, until October 1, 1941. But the Trust was insolvent, as the Court found, at all times from at least December 31, 1937, and by December 31, 1941, which was just about the time the Hanlon Group came in, the asset value of a $1,000. debenture was at its all time low of $362.66. Hence, there was no time during the incumbency of the Hanlon Group that the Trust was in a financial position to redeem the bonds, and even if the Hanlon Group had been most faithful to the Trust, they could not have paid off the debentures, even if they had wanted to.

This exposes the error in the reasoning of the learned District Judge, that viewing the Trust as at the time when this action was first filed

> "the trustees [of Aldred] should have exercised the 'option' of redeeming the debentures and closing the Trust,"

and that since the trustees failed to do what they should have done, the Court's order of liquidation

> "should be interpreted as the act of those who were appointed to exercise properly the option to redeem in place of the former trustees who would not."

The learned Circuit Court of Appeals naturally declined to accept this reasoning, because the simple and undeniable fact is that there never was a moment when the "former trustees" could have redeemed the debentures.

We hold no brief for the Hanlon Group, or for the trustees elected by the stock owned by it. They were guilty of wrongdoing and deserved to be removed. We fail to see, however, how that fact can have any relevance in determining the meaning of the words "at the option" in the Indenture. The meaning of those words must be determined not by the conduct, good or bad, of the Hanlon Group, but by the terms of the Indenture, which was executed about fourteen years before the Hanlon Group acquired control.

Irrespective of the fidelity or the infidelity of the Hanlon Group, the words "at the option" of Aldred mean "at the election" of Aldred. No such election was exercised here, and because of the financial condition of the company it could not have been exercised. Payment was made pursuant to a court order entered over the opposition of Aldred. This could not constitute a redemption "at the option" of Aldred.

POINT II

The modification of the judgment so as to permit stockholders to continue the trust with their own money, if they so elect, cannot confer on the debenture holders any contractual right to the call premium because, by the terms of the Indenture, that right depends, not on whether or not the trust is continued after redemption of the debentures, but solely on whether or not the debentures were called "at the option" of Aldred. The modification affects only the rights of stockholders, and does not convert the redemption of the debentures from one by judicial compulsion into one at the option of Aldred.

At the time the debenture holders committee moved for an order directing the Receivers to "purchase and retire" the debentures, they prayed that the Receivers be directed to pay the face amount with accrued interest "plus a premium of 5% of the principal amount thereof" (R. 29). That motion was granted only to the extent of directing the Receivers to pay the face amount with accrued interest; they were not given leave to pay the call premium (R. 29, 30, 31).

Petitioners now intimate (Brief, p. 5) that the application for leave to pay the premium was properly denied because the denial "was predicated upon the assumption that the Trust would be fully liquidated."

It is difficult to see how a different formula can be justified merely because the stockholders have now been given permission to continue the Trust with their own money after the debenture holders have been paid. By the terms of the Indenture, the right to call premium depends not

upon the continuance or the termination of the Trust structure, but solely upon whether or not there was a redemption "at the option" of Aldred. A redemption at the option of Aldred would entitle debenture holders to the call premium, whether the Trust continues or not; by the same token, debenture holders would not be entitled to the call premium if redemption were not at the option of Aldred, whether the Trust continues or not.

The learned Circuit Court of Appeals summed up the situation succinctly and accurately in these words (44):

> "The trust in effect was given an option of either liquidating or continuing without the bonds. The fact that the majority stockholders decided to continue instead of to dissolve does not make the redemption of the bonds voluntary. In either event the bonds would be completely paid off as a result of judicial compulsion."

That there has been no call at the option of Aldred was recognized by those of the debenture holders who intervened in the District Court. In their brief they said:

> "Although no technical call of the debentures for redemption has occurred, the standards of fairness and equity in receivership require that the court accomplish a like result."

Whether "fairness and equity" require that the Court award the debenture holders about $300,000. in addition to what they are entitled to by their contract is an entirely different question, which we discuss in the succeeding point.

POINT III

The Indenture is the source and the measure of the debenture holders' rights. Hence there can be no justification for giving them, on "equitable" grounds, a call premium not authorized by the Indenture. But even if "equities" could displace the rights and limitations created by the Indenture, there are no "equities" here in favor of the debenture holders. Aldred did not seek to eliminate the debenture holders: they have been paid out upon their own insistence that they be relieved of a speculative investment and of any further risks in connection with the operation of what they believed to be a "doomed enterprise." Payment made under such circumstances carries with it no "equity" to a bonus.

Before discussing the question of "equities", it should be noted that whether or not the debenture holders are entitled to a call premium is not a matter of "equities", but solely a matter of contract. We have already seen that no such contract right exists, and, as the learned Court below well said (42-3):

> "The rationale of fair and equitable is recognition of contractual rights."

But even if an award unauthorized by the Indenture would be proper in a case where there were "equities" in favor of the debenture holders, there would be no justification for such an award in the circumstances of this case.

The only "equity" suggested by the debenture holders in the Court below was that redemption was made necessary

by the manipulations of the Hanlon Group, and that the "Bailey Group"—these Respondents—"is in no better position" because they bought the Hanlon Group stock after the Circuit Court of Appeals had affirmed the order removing the Hanlon Group. This contention had been adopted by the learned District Judge, who paraphrased the argument by saying that the present free stockholders bought "into the middle of a lawsuit" with knowledge of "the taint" which the stock had acquired in the hands of the previous owners, and though the District Court assumed that the prior owners had no present interest in the stock, he said (R. 18):

> "Nevertheless, in measuring the equities between the debenture holders, who were the persons defrauded by the activities of the former owners of the free shares, and the trustees elected by those shares, I am inclined to think that the Court should recognize the situation in its entirety and not be bound by too narrow a construction of what is meant by the option of the Trust in calling the debentures. It was necessary for the Securities & Exchange Commission, an independent governmental agency, to seek a court order, which, in substance, called for the liquidation of this Trust. When the Court ordered the liquidation of the Trust there were no trustees to exercise the option. In such a situation equity and good conscience call for the payment of the premium to the debenture holders" (R. 18, 19).

The foregoing, we submit with great respect, is a perfect *non sequitur*, and was properly rejected by the Circuit Court of Appeals.

There has never been any dispute about the fact that the present free shareholders were bona fide purchasers of the stock at arms' length; that they never had anything to do with the Hanlon Group or its machinations, and that since Respondents' purchase of the stock the Hanlon Group has never had anything to do with the management or the Respondents.

Granted the infidelity of the Hanlon Group, that infidelity was personal to them; it gave the right to remove them from their offices, as has been done. But it resulted in no "taint" of their stock which would make a subsequent bona fide purchaser thereof, or the remaining shareholders who did not purchase from the Hanlon Group, chargeable, either in "equity and good conscience" or otherwise, with the iniquity of the prior management, or justify the taking of shareholders' money and giving it to debenture holders contrary to the provisions of the Indenture.

Yet, it is upon such a premise, and only upon such a premise, that the District Judge rejected the plain rule of the authorities and the clear language of the Indenture, and evolved an "equitable" basis upon which Respondents were to be vastly penalized for doing what they want with their own money—and the debenture holders rewarded with a premium at Respondents' expense. It is not surprising that the Circuit Court of Appeals declined to accept such fallacious reasoning.

There was still another flaw in the reasoning of the learned District Judge. The "equities", if any, on March 22, 1948, when the order granting the premium was made, were precisely those which existed on June 19, 1947, when the same Judge made the order denying the premium. If there were any moral infirmity, any "taint", in appellants' position in March 1948, it would have been equally present

in June 1947. As early as April 29, 1946, in denying appellants' motion to defer the sale of the Eastern Racing Association stock, the learned District Judge wrote:

> "The petitioners state that they are bona fide purchasers and holders of this stock, and have no tie-in agreements with the former owner. For the purposes of this decision, I will accept that statement at its face value and assumed it to be a fact. However, I cannot overlook the fact that, regardless of the circumstances and conditions under which they purchased the stock, they nevertheless bought into a law suit."

Thus, what was referred to by the learned District Judge as a "taint" creating an "equity" in favor of the debenture holders, was not something which emerged subsequent to June 19, 1947. Yet, on June 19, 1947, these "equities" were not sufficient to justify an award of the premium for "redemption". We are, of course, not arguing that there was any such "equity" at that time; we are pointing out merely that nothing has happened since that time to create an equity.

The purpose of the redemption clause is clear: it was to give Aldred the right to pay off the indebtedness in advance of its due date, in the event that Aldred was financially able, and should deem it profitable to do so. But since such a payment might deprive a debenture holder, against his will, of the benefit of a sound, long-term investment at a better rate than he might obtain on reinvestment, the right to redeem is coupled with an obligation to pay the debenture holder a premium to compensate him for the deprivation.

None of the circumstances contemplated by the provision for the payment of a premium is present here.

The learned Court below was clearly right in saying (44):

> "Payment was made against the desire of the Trust; it was not made in order to take advantage of favorable conditions; payment was at the request of the bondholders and they were not deprived of a favorable investment. We think that the redemption of the bonds was not within either the letter or the spirit of the indenture language."

Thus, in addition to the fact that there has been no redemption "at the option" of Aldred—the condition precedent to the payment of a call premium, as provided in the Indenture—there is present here no "equity" which could justify its payment.

CONCLUSION

The Petition for Certiorari should be denied.

Respectfully submitted,

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